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September 23, 2003

The Honorable William H. Donaldson
Chairman
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Ms. Linda D. Fienberg
President
NASD Dispute Resolution
1735 K Street, N.W.
Washington, D.C. 20006

Mr. Robert S. Clemente
Director, Arbitration
New York Stock Exchange, Inc.
20 Broad Street
New York, New York 10005

Dear Chairman Donaldson, Ms. Fienberg, and Mr. Clemente:

We are writing with respect to the August 29, 2003, report, Employment Disputes: Recommendations to Better Ensure that Securities Arbitrators Are Qualified, GAO-03-790, which was prepared by the U.S. General Accounting Office (GAO) at our request. It evaluates the characteristics and outcomes of arbitrated employment and employment discrimination disputes, and actions taken by the Securities and Exchange Commission (SEC), NASD, and the New York Stock Exchange (NYSE) since the previous GAO report, Employment Discrimination: How Registered Representatives Fare in Discrimination Disputes, GAO/HEHS-94-17/ March 30, 1994. The 1994 report called for reforms in the selection and operation of securities arbitration panels and improved oversight of the arbitration process by the SEC.

GAO noted on page 9 of the 1994 report that: "Perceptions of the fairness of the arbitration process depend on the impartiality and competence of the arbitrators who decide the cases." We wholeheartedly agree, particularly in this context where, as GAO stresses on page 1 of the 2003 report:

> Arbitrators have the authority to make legally binding decisions that can only be appealed on limited grounds. Their decisions can have serious consequences for an employee's career or livelihood since employee cases can involve such issues as salary, performance evaluations, and alleged discrimination.

Against this backdrop, the 50-page report that we are releasing today found that the SEC and the self-regulatory organizations (SROs) have made significant progress in addressing a number of shortcomings in their respective programs, but GAO also determined that additional improvements could be made. Our specific comments on the report are as follows:

1. GAO found that both NASD and NYSE have policies and procedures intended to promote fair arbitration, but important differences persist. For example, the NYSE only arbitrates discrimination claims when all parties agree to arbitration after the dispute occurs, while the NASD has continued to arbitrate disputes based on agreements employees must sign as a condition of employment (p. 7). In 1997, the Equal Employment Opportunity Commission (EEOC), which is responsible for enforcing the nation's discrimination laws, published a policy statement opposing the use of mandatory arbitration agreements for discrimination disputes. We agree with the EEOC and urge that immediate action be taken to end the NASD practice of arbitrating disputes based on such agreements. It is unfair to force employees into arbitration of a sexual harassment or race or age discrimination claim as a condition of employment, and the SEC and the NASD should not by their action or inaction sanction such a practice.

2. Both NASD and NYSE require that all applicants for the arbitrator roster provide information on their affiliation with the securities industry, have five years of work experience, and supply two letters of recommendation (p. 10). At NASD, applicants must take a half-day introductory training course, be evaluated by the trainer, and pass a written test on arbitration procedures. At the NYSE, on the other hand, the applicant is considered able to arbitrate any case once he or she participates in one training course (p. 11). GAO says that "ongoing training at both SROs is limited" (p. 11) and that information from arbitrator applicants not employed in the securities industry is not checked by the SROs (p. 10). GAO indicates that NYSE requires arbitrators to attend at least one training course every four years, while NASD only offers chairperson training. NASD is proposing a rule change that would require the verification of background information on all new arbitrators (p. 10, footnote 25). The NYSE, however, contends that additional verification of the arbitration pool would be too costly -- "the costs . . . significantly exceed the benefits that would be gained" -- and that counsel often conduct their own independent due diligence and verification of qualifications (pp. 47-48). We are troubled by these findings and urge prompt action to improve the programs and procedures designed to ensure that arbitrators are qualified and perform well.

3. GAO found that both NASD and NYSE have developed procedures for evaluating arbitrator performance, but these evaluations are not received on a routine basis, with troubling consequences. GAO reviewed the records of 124 of the 494 NASD arbitrators who heard employment and/or discrimination cases between January 2001 and June 2002, and estimated that 45 percent of arbitrators who heard cases during this time received some type of evaluation and of those only two percent received all three types -- peer, party, and NASD staff (p. 14). NASD rates arbitrators on a three-point scale on a quarterly basis, but GAO found that these ratings "are often based on little or no information" (p. 15). NASD reported that any arbitrator who did not have any evaluations during the quarter is likely to be rated adequate or "2." GAO found that 57 percent of arbitrators with a 2 rating had not received any evaluations during this time frame, and some arbitrators without evaluations were also rated excellent. The GAO report states at page 33 that NYSE officials indicated that NYSE has evaluation procedures similar to NASD and reported that its staff generally evaluate active arbitrators at least once a year, but GAO was "unable to confirm this information." This is unacceptable and we urge all parties to redouble their efforts to address serious shortcomings in the operation and effectiveness of the rating systems.

4. In reviewing the records of NASD arbitrators, GAO found that staff did not always document how they responded to poor evaluations and complaints (p. 16). For example, one arbitrator, who had been permanently dropped in 2001, appeared to have complaints going back to 1993, yet no changes had been made to his adequate rating of 2 (p. 17). We are concerned that this sloppiness undermines the integrity of the assessment process to the detriment of claimants.

5. GAO indicates that, since 1995, the SEC has examined NASD's and NYSE's arbitration programs three times each, and beginning in 1998, SEC began to review employment cases (p. 29). SEC cited problems at one or both SROs in the procedures used to (1) ensure arbitrators are qualified and (2) track arbitrator performance. In response, SEC staff recommended that steps be taken to:

- ensure that they consistently conduct CRD checks of all industry arbitrators and document those reviews in arbitrator profiles;
- ensure that all arbitrator profiles are complete and reflect new or updated information arbitrators submit about themselves;
- lengthen training courses for new arbitrators;
- include in arbitrator training manuals guidance on certain arbitration procedures and certain problems arbitrators are likely to encounter;

- develop policy on how often arbitrators must attend ongoing training, the circumstances under which it can be waived, and documentation of reasons waivers are granted;

- ensure that all pertinent information on arbitrator performance, whether negative or positive, is recorded in a central database; and

- do more to address complaints of poor arbitrator performance, including, if appropriate, removing arbitrators from the active pool and better documenting actions taken in response to complaints of poor performance.

GAO and SEC indicate that the SROs have taken steps to address these recommendations, and SEC says it will follow up on these matters in ongoing inspections (p. 32). We commend the SEC and SROs for their actions, strongly agree with SEC's recommendations, and ask GAO to monitor this activity and inform us in a followup report whether these issues have been resolved in a timely and effective manner.

6. To help ensure that only qualified arbitrators hear employment and employment discrimination cases at NASD and NYSE, GAO recommends that SEC direct the two SROs to verify basic background information of all new applicants for their arbitrator rosters. GAO also recommends that SEC continue to review the adequacy of procedures for evaluating arbitrator performance in their next inspections at NASD and NYSE. We agree with these recommendations as well and urge their implementation.

7. GAO reports that, of the 1,546 employment cases decided by arbitrators at NASD and NYSE over the last 10 years (January 1993 through June 2002), 261 (17 percent) included at least one discrimination claim. NASD arbitrated 202 of those cases. The number of discrimination claims has generally decreased in recent years. Age (33 percent) and sex-based (32 percent) were the most prevalent discrimination claims. Cases with discrimination claims required more hearing sessions and took longer to complete than those with no discrimination claims. Claimed amounts were generally higher at the NYSE. In over half of all employment cases, employees won some level of monetary compensation, although in cases with discrimination claims employees were generally less likely to win. When employees won, they received less than half of the compensatory damages claimed. When compensatory damages were awarded in discrimination cases, it tended to be higher than compensatory damages awarded in other employment cases. *See* charts and discussion at pages 17-28. GAO's analysis does not include cases that were settled or withdrawn, which happens, according to NASD, in 60 percent of all cases. These findings further underscore our concern about allowing the NASD practice of arbitrating discrimination cases based on mandatory pre-dispute arbitration agreements to continue.

Reports suggest that discrimination continues to be a problem on Wall Street and that remedies need to be strengthened. *See*, e.g., "Up Against The Wall," St. Petersburg Times, Monday, February 24, 2003; and Susan Antilla, Tales From The Boom-Boom Room: Women vs. Wall Street (Bloomberg Press, 2002). The integrity and fairness of the arbitration process, including ongoing training for arbitrators in employment and discrimination law and policies and prompt weeding out of biased or poor arbitrators, are important components. We stand ready to support these endeavors. At the same time, we also continue to believe that the public interest would best be served if arbitration were used to resolve employment disputes only if both parties agreed to use arbitration after the dispute had arisen. In this way, no one in the securities industry would be forced as a condition of employment to preemptively sign away their right to have a future racial discrimination, age discrimination, or sexual harassment claim adjudicated in the courts.

Thank you for your cooperation and attention to this matter. We are sharing this information with Chairman Oxley and Ranking Member Frank of the Committee on Financial Services, which now has jurisdiction over securities and exchanges, Chairman Boehner and Ranking Member Miller of the Committee on Education and the Workforce, which has jurisdiction over workforce protections generally, and Chairman Sensenbrenner and Ranking Member Conyers of the Committee on the Judiciary, which has jurisdiction over anti-discrimination laws, for any action they deem appropriate.

Sincerely,

John D. Dingell

JOHN D. DINGELL
RANKING MEMBER
COMMITTEE ON ENERGY AND COMMERCE

Edward J. Markey

EDWARD J. MARKEY
RANKING MEMBER
SUBCOMMITTEE ON TELECOMMUNICATIONS AND THE INTERNET

Enclosure

cc: The Honorable David M. Walker, Comptroller General
U.S. General Accounting Office

The Honorable W.J. "Billy" Tauzin, Chairman
Committee on Energy and Commerce

The Honorable Michael G. Oxley, Chairman
Committee on Financial Services

The Honorable Barney Frank, Ranking Member
Committee on Financial Services

The Honorable John A. Boehner, Chairman
Committee on Education and the Workforce

The Honorable George Miller, Ranking Member
Committee on Education and the Workforce

The Honorable F. James Sensenbrenner, Jr., Chairman
Committee on the Judiciary

The Honorable John Conyers, Jr., Ranking Member
Committee on the Judiciary